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ARIZONA CORPORATION COMMISSION



Arizona Corporation Commission

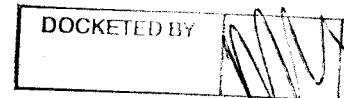
DOCKETED

SEP 04 2007

DATE: SEPTEMBER 4, 2007

DOCKET NO: W-01303A-05-0718

TO ALL PARTIES:



Enclosed please find the recommendation of Administrative Law Judge Teena Wolfe. The recommendation has been filed in the form of an Opinion and Order on:

ARIZONA-AMERICAN WATER COMPANY
(FINANCING)

Pursuant to A.A.C. R14-3-110(B), you may file exceptions to the recommendation of the Administrative Law Judge by filing an original and ten (10) copies of the exceptions with the Commission's Docket Control at the address listed below by 4:00 p.m. on or before:

SEPTEMBER 13, 2007

The enclosed is NOT an order of the Commission, but a recommendation of the Administrative Law Judge to the Commissioners. Consideration of this matter has tentatively been scheduled for the Commission's Working Session and Open Meeting to be held on:

SEPTEMBER 18, 2007 AND SEPTEMBER 19, 2007

For more information, you may contact Docket Control at (602) 542-3477 or the Hearing Division at (602) 542-4250. For information about the Open Meeting, contact the Executive Director's Office at (602) 542-3931.

A handwritten signature in black ink, appearing to read "Brian C. McNeil".

BRIAN C. McNEIL
EXECUTIVE DIRECTOR

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AZ CORP COMMISSION
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1 **BEFORE THE ARIZONA CORPORATION COMMISSION**

2 **COMMISSIONERS**

3 MIKE GLEASON - Chairman
4 WILLIAM A. MUNDELL
5 JEFF HATCH-MILLER
6 KRISTIN K. MAYES
7 GARY PIERCE

8 IN THE MATTER OF THE APPLICATION OF
9 ARIZONA-AMERICAN WATER COMPANY FOR
10 APPROVALS ASSOCIATED WITH A
11 TRANSACTION WITH THE MARICOPA
12 COUNTY MUNICIPAL WATER
13 CONSERVATION DISTRICT NUMBER ONE.

DOCKET NO. W-01303A-05-0718

DECISION NO. _____

14 **OPINION AND ORDER**

15 DATE OF HEARING:

March 2, 2006 (Pre-hearing Conference); August 1, 2006, September 14, 2006 (Procedural Conferences); December 21, 2006 and March 15, 2007 (Pre-hearing Conferences); March 19, 20, 21 and 26, 2007 (Hearing).

16 PLACE OF HEARING:

Phoenix, Arizona

17 ADMINISTRATIVE LAW JUDGE:

Teena Wolfe

18 APPEARANCES:

Kristin K. Mayes, Commissioner, Arizona Corporation Commission

Keith A. Layton, Kevin Torrey and Charles Hains, Staff Attorneys, Legal Division, on behalf of the Arizona Corporation Commission's Utilities Division;

Scott Wakefield, Chief Counsel, and Daniel Pozefsky, Staff Counsel, on behalf of the Residential Utility Consumer Office;

Craig A. Marks, CRAIG A. MARKS, P.L.C., on behalf of Arizona-American Water Company;

Michele L. Van Quathem, RYLEY, CARLOCK & APPLEWHITE, P.A., on behalf of Pulte Homes Corporation;

Jeffrey W. Crockett and Bradley S. Carroll, SNELL & WILMER, L.L.P., on behalf of CHI Construction Company, Inc., Courtland Homes, Inc., Taylor Woodrow/Arizona, Inc., and Fulton Homes Corporation;

Franklyn D. Jeans, BEUS GILBERT, P.L.L.C.,
on behalf of Suburban Land Reserve, Inc. and
Fulton Homes Corporation;

Brian J. Schulman and Melissa Goldenberg,
GREENBERG TRAURIG, on behalf of Trend
Homes;

Derek L. Sorenson, QUARLES BRADY
STREICH LANG, on behalf of
Westcor/Surprise, L.L.C.; and

Michael W. Patten and Timothy J. Sabo,
ROSHKA, DEWULF & PATTEN, P.L.C., on
behalf of Maricopa County Municipal Water
Conservation District Number One.

BY THE COMMISSION:

I. PROCEDURAL HISTORY

A. INITIAL APPLICATION

On October 11, 2005, Arizona-American Water Company ("Arizona-American" or "Company") filed with the Arizona Corporation Commission ("Commission") the above-captioned application. The application requested certain approvals associated with a transaction with the Company's Agua Fria Water District and the Maricopa County Municipal Water Conservation District Number One ("MWD") in order to enable the Company to obtain treatment of a portion of the Company's Central Arizona Project ("CAP") water allocation at a planned regional water treatment facility. The October 2005 application stated that MWD proposed to construct a regional water-treatment facility known as the White Tanks Regional Water Treatment Facility to treat surface water delivered over CAP facilities. In association with the planned transaction with MWD, the Company requested Commission approval of the issuance of evidence of indebtedness in the amount of approximately \$37,414,000 for a 40-year capital lease obligation with an interest rate of 275 basis points over the long-term Treasury Bond rate; approval of the transfer of certain assets to MWD; and approval of proposed increases to and extension of the Company's existing Water Facilities Hook-Up Fee Tariff assessed to new-home construction. In association with the capital lease, the Company also sought Commission approval of its proposed ratemaking treatment and recovery method for capital and operating costs, and a prudence finding.

By Procedural Order issued December 19, 2005, a procedural schedule was set for the

1 processing of the application, which included a hearing on the application, public notice
2 requirements, and intervention deadlines. The Residential Utility Consumer Office ("RUCO")
3 requested and was granted intervention. No other intervention requests were filed at that time. On
4 February 10, 2006, RUCO filed direct testimony on the October 11, 2005 application, and the
5 Commission's Utilities Division Staff ("Staff") filed a Staff Report on the October 11, 2005
6 application.

7 On March 2, 2006, at the Pre-Hearing Conference, the Company indicated that issues had
8 arisen between the Company and MWD, and requested that the procedural schedule in this matter be
9 suspended pending their resolution. By Procedural Order issued March 2, 2006, the Company's
10 request to suspend the procedural schedule was granted.

11 **B. REVISED APPLICATION**

12 Following the March 2, 2006, suspension of the procedural schedule, the Company filed
13 several status reports. A Procedural Conference was convened on August 1, 2006. The Company,
14 RUCO and Staff attended and discussed procedural issues related to the processing of the Company's
15 application.

16 On September 1, 2006, the Company filed a Revised Application in this docket. The Revised
17 Application indicates that the Company plans to construct a White Tanks Regional Water Treatment
18 Facility ("White Tanks Project"), not in association with MWD. The Revised Application requests,
19 for the Company's Agua Fria District, relief in the form of an adjustment to its existing Water
20 Facilities Hook-Up Fee for new home construction. The Revised Application also requests
21 accounting orders related to the planned water treatment facility, and requests that the Company be
22 ordered to make certain associated filings as a part of its previously-ordered 2008 rate case filing for
23 its Agua Fria District.

24 On October 27, 2006, Staff filed a Staff Report and Staff Recommended Order,
25 recommending approval of the Company's proposed hook-up fee and accounting order as requested
26 in the Revised Application.

27 Between October 23, 2006 and December 6, 2006, Applications to Intervene in this
28 proceeding were filed by Pulte Homes Corporation ("Pulte"), CHI Construction Company, Inc.

1 (“CHI”), Courtland Homes, Inc. (“Courtland”), Taylor Woodrow/Arizona Inc. (“Taylor Woodrow”),
2 Trend Homes, Inc. (“Trend”), Fulton Homes Corporation (“Fulton”), Suburban Land Reserve, Inc.
3 (“Suburban”), and Westcor/Surprise, LLC (“Westcor/Surprise”) (jointly, “Developers”).

4 On November 8, 2006, MWD filed an Application for Leave to Intervene. Initially, the
5 Company opposed MWD’s intervention, but withdrew its opposition in its November 29, 2006
6 Request for Expedited Hearing.

7 The hearing in this matter convened as scheduled on March 19, 2007, before an authorized
8 Administrative Law Judge of the Commission, and concluded on March 26, 2007. The parties
9 appeared through counsel, presented testimony, and cross-examined witnesses.

10 Following the hearing, on March 28, 2007, MWD filed Late-Filed Exhibits D-52 and D-53.
11 Arizona-American, Pulte, Trend, CHI, Courtland, Taylor/Woodrow, Fulton, Suburban, Westcor,
12 MWD, RUCO, and Staff filed closing briefs, and Arizona-American, CHI, Courtland,
13 Taylor/Woodrow, Trend, MWD, and RUCO filed reply briefs. On April 30, 2007, Arizona-
14 American filed a Supplement to Reply Brief. The matter was subsequently taken under advisement
15 pending the submission of a Recommended Opinion and Order to the Commission.

16 **II. POSITIONS OF THE PARTIES**

17 **A. ARIZONA-AMERICAN**

18 Arizona-American states that continued reliance solely on groundwater in its Agua Fria Water
19 District would be imprudent due to accelerated groundwater level declines, land subsidence,
20 declining well production rates, and the increasing number of wells not meeting Safe Drinking Water
21 Act water quality standards (Revised Application, Exh. A-2 at 3-4). The Regional Water Supply Plan
22 released by WESTCAPS¹ in April 2001 concluded that the area’s water suppliers should maximize
23 use of CAP water and other surface water resources, and recommended the construction of regional
24 treatment facilities to treat that water (Exh. A-2 at 4-5).

25
26 ¹ According to the mission statement on its website, “WESTCAPS is a coalition of CAP subcontractors most of whom
27 serve drinking water to communities in the west Salt River Valley. WESTCAPS’ mission is to develop workable
28 alternatives for its members to provide their customers with a cost effective, sustainable, reliable, and high quality water
supply through partnerships and cooperative efforts in regional water resource planning and management, emphasizing
CAP utilization” (See <http://www.westcaps.org/public/default.cfm>). The website lists Arizona-American as a member of
WESTCAPS, and lists MWD as an advisor to WESTCAPS.

Arizona-American holds a CAP water subcontract for 11,093 acre-feet per year, and has designed the White Tanks Project to treat CAP water for distribution to its customers in its Agua Fria District (*Id.*). The Company has a construction contract in place for construction of the plant (Direct Testimony of Joseph E. Gross, Exh. A-4 at 4) and permitting of Phase I of the plant is essentially complete (Exh. A-2 at 6). The White Tanks Project is designed to treat 13.5 million gallons per day ("MGD") in Phase I(a). It is expandable to 20 MGD in Phase I(b) with the addition of one more treatment-unit train, and eventually the White Tanks Project can accommodate the addition of three additional 20 MGD phases, for a total treatment capacity of 80 MGD at the 45-acre plant site (*Id.* at 5-6). Arizona-American purchased the White Tanks Project site in 2002 after WESTCAPS identified the site for a treatment facility based on its canal location and its proximity to multiple water provider service areas (*Id.* at 5).

Arizona-American's witness testified that the Company has spent more than six million dollars for land acquisition, the completed design, permitting, company labor and overhead, and has spent over ten million dollars on a completed thirteen mile long north-south water transmission main which will deliver treated water from the White Tanks Project to other transmission mains located throughout the Agua Fria District service area (Exh. A-4 at 5). Arizona-American projects that the White Tanks Project will be needed in May 2009 to meet expected customer demand for summer 2009 (*Id.* at 6).

1. Water Facilities Hook-Up Fee

The Company requests that the Commission increase the existing Water Facilities Hook-Up Fees applicable in the Company's Agua Fria Water District, based on the fair-value finding for the Agua Fria District in Decision No. 67093 (June 30, 2004), as follows:

	<u>Existing</u> <u>Water Facilities</u> <u>Hook-Up Fee</u>	<u>Proposed</u> <u>Water Facilities</u> <u>Hook-Up Fee</u>
<u>Meter Size</u>		
5/8 x 3/4-inch	\$ 1,150	\$ 3,280
3/4-inch	1,725	4,920
1-inch	2,875	8,200
1 1/2-inch	5,750	16,400
2-inch	9,200	26,240
3-inch	18,400	52,480
4-inch	28,750	82,000
6-inch or larger	57,500	164,000

1 Arizona-American believes that its proposal to finance the White Tanks Project with hook-up
2 fees, which will be treated as contributions in aid of construction ("CIAC"), is equitable because
3 customer growth is largely driving the need for the plant (Surrebuttal Testimony of Thomas M.
4 Broderick, Exh. A-7 at 7). The Company asserts that the amount of the hook-up fee increase it is
5 requesting is reasonable because it is in line with fees charged by West Valley municipal water
6 providers (*See* Exh. A-2 at 9-10; *See also* Direct Testimony of Mike Brilz, Exh. P-1 at 5 and
7 attached Exhibit).

8 **2. Accounting Requests**

9 a. Post-in-Service Allowance for Funds Used During Construction
10 ("AFUDC")

11 Arizona-American requests that the Commission authorize the Company to record post-in-
12 service AFUDC on the excess of the construction cost of the White Tanks Project (including
13 development, site acquisition, design, company labor, overheads, and AFUDC) over the amount of
14 directly related hook-up fees collected through December 31, 2013, or the date that rates become
15 effective subsequent to a rate case that includes 80 percent (based on estimated cost) of the White
16 Tanks Project in rate base, whichever comes first.

17 The application states that when the plant is completed, there will still be a significant
18 shortage between capital expenses and hook-up fees (Exh. A-2 at 11). The Company requests the
19 ability to book post-in-service AFUDC in order to keep it whole on its investment until such time that
20 the accumulated hook-up fees are sufficient to fund the entire plant balance. This treatment will not
21 affect customer rates because the additional post-in-service AFUDC will later be completely offset by
22 hook-up fee funds.

23 b. Rate Base – Excess Contribution Exclusion

24 Arizona-American requests authorization to exclude from rate base the contribution balance
25 of hook-up fees directly related to the White Tanks Project collected subsequent to the effective date
26 of a decision in this case over the aggregate of (1) construction expenditures (including development,
27 site acquisition, design, company labor, overheads, and AFUDC) for the same period that are
28 included in rate base and (2) any costs deemed imprudently incurred from contributions used to

1 calculate rate base until December 31, 2013.

2 The Company states that because construction work in progress ("CWIP") is not typically
3 included in rate base, the collected hook-up fees should not be considered to be CIAC until a
4 corresponding amount of plant, funded by hook-up fees, enters service (Exh. A-2 at 11). Otherwise,
5 the CIAC balance would grow faster than rate base, causing rate base to decline rapidly as hook-up
6 fees are collected, only to then bounce back as plant enters service (*Id.*).

7 **3. 2008 Rate Filing Requirements**

8 a. Revised Hook-Up Fee Proposal

9 Arizona-American requests that the Commission require Arizona-American, as part of its
10 2008 Agua Fria rate case filing, to include a proposal to adjust the Water Facilities Hook-Up Fee
11 Tariff, based on information known to that date, including:

- 12 1) Actual to-date and remaining plant costs;
- 13 2) The effects of any third-party treatment contracts;
- 14 3) Actual hook-up fee collections;
- 15 4) Revised projected customer additions and meter preferences;
16 and
- 17 5) Future Agua Fria Water District capital requirements.

18 The Company states that this will allow the Commission to reset the hook-up fees as
19 necessary, based on the best information available at the time.

20 b. Operation and Maintenance ("O&M") Expense Recovery Mechanism

21 Arizona-American requests that the Commission require Arizona-American, as part of its
22 2008 Agua Fria rate case filing, to include a proposed mechanism, similar to the Commission's
23 arsenic cost recovery mechanism ("ACRM") procedure, to defer and subsequently recover O&M
24 expense incurred for the White Tanks Project until such expenses can be placed in base rates.

25 The Company estimates that the O&M costs for the White Tanks Project will be
26 approximately \$1.5 million per year, base on current media, electricity, and other costs.

27 **4. MWD Treatment Facility**

28 Arizona-American requests that the Commission find that it would be imprudent for Arizona-

1 American, instead of building its own water treatment facility, to purchase treatment services from
2 MWD at the water treatment facility MWD has proposed in this proceeding. Arizona-American
3 disagrees with MWD's assertion that its plant will cost less than Arizona-American's, and believes
4 that MWD's cost estimate is seriously flawed. In addition, Arizona-American states that the
5 proposed MWD plant site would require Arizona-American to construct additional interconnection
6 facilities, which would increase Arizona-American's costs.

7 The Company calculates that MWD proposal to build a treatment plant and have Arizona-
8 American purchase treatment capacity would require a large rate increase (an additional
9 \$21.07/month) for all of Arizona-American's customers (Surrebuttal Testimony of Thomas
10 Broderick, Exh. A-7 at 6). Arizona-American argues that if it were to purchase capacity from MWD
11 and construct the additional facilities that would be required to make such a purchase possible, the
12 Company would have to file a rate application in order to recover the increased costs (*Id.* at 7-8), and
13 would experience regulatory lag in the cost recovery.

14 Arizona-American argues that MWD's assertions that building the plant with hook-up fee
15 financing would harm the Company's financial strength are speculative and not supported by the
16 evidence in this proceeding. The Company also disagrees with MWD's opinion that the hook-up fee
17 proposal would violate the fair value requirement of the Arizona Constitution, and points out that the
18 Company is seeking to increase the amount of the current hook-up fee, which was initiated outside a
19 rate case, based on the fair value finding in Decision No. 67093 (June 30, 2004). The Company
20 states that its proposal to finance the White Tanks Project with hook-up fees places the costs on new
21 customers, whose addition to the system is causing the need for the plant. Arizona-American
22 believes this is preferable to placing the costs on both existing and new customers, which it asserts
23 would be the result if Arizona-American were to purchase treatment capacity from an MWD plant
24 (*Id.* at 7).

25 The Company is also concerned with the possibility that a capacity commitment for a large
26 portion of an MWD plant would require the agreement to be treated as a capital lease, in which case
27 the lease asset would be included in rate base to recover the asset as well as lease costs, further
28 exacerbating the rate burden on customers and the regulatory lag impact on the Company (Co. Br. at

1 20-21).

2 Arizona-American further asserts in support of its position that the proposed MWD plant has
3 yet to be designed; MWD's proposed construction schedule is overly optimistic and unreliable due to
4 the conceptual nature of the proposed plant; Arizona-American would not be the operator of MWD
5 plant; MWD's irrigation wells would not provide back-up water drinking water supplies without
6 extensive additional treatment costs; the proposed MWD plant site would eventually require costly
7 expansion of the Beardsley Canal; MWD lacks experience in designing, operating, or constructing
8 potable water treatment facilities; MWD has not acquired customers for its proposed plant; and
9 MWD has no obligation to construct the plant and is not subject to the Commission's jurisdiction (*Id.*
10 at 21-28).

11 Arizona-American also states that requiring Arizona-American to deal with MWD would put
12 the Company in a disadvantageous bargaining position (*Id.* at 28-29). Arizona-American opposes
13 each item of relief requested by MWD in this proceeding.

14 **B. MWD**

15 MWD states that it has a demonstrated history of providing essential and reliable water and
16 electric services at low cost, and asserts that it will bring its record of service of more than 75 years to
17 its plans to construct a regional water treatment plant for Phoenix's West Valley. MWD asserts that
18 its service area is rapidly changing, that it must adapt in order to continue to fulfill its purpose of
19 serving its landowners, and that part of MWD's response to the changes in its service area is
20 construction of a regional surface water treatment plant. MWD states that it plans to utilize the plant
21 to treat its own Agua Fria surface water, which must be used for the benefit of the landowners of
22 MWD.

23 MWD's witness testified that MWD will build the plant regardless of other customers it may
24 serve (Surrebuttal Testimony of James R. Sweeney, Exh. D-46 at 3). MWD states that it would
25 provide treatment services to Arizona-American for the Company's CAP allocation if it reaches an
26 agreement with Arizona-American. MWD has not finalized any service contracts, but its witness
27 testified that MWD is in "an advanced state of discussions" with the City of Goodyear, which has
28 given a verbal commitment to the project, subject to working out a satisfactory contract, to treat that

1 city's CAP allocation (Direct Testimony of James R. Sweeney, Exh. D-45 at 5). MWD states that it
2 will contract with other water providers in the area who desire treatment services (*Id.*).

3 MWD states that Arizona-American has not provided it with a firm price for treatment of
4 MWD's surface water (MWD Reply Br. at 8), but argues that its planned plant will cost less than the
5 plant proposed by Arizona-American (MWD Br. at 9-11). MWD asserts that its plant will have
6 lower construction costs, lower operating costs, and lower financing costs than Arizona-American.
7 MWD also states that it would provide a "landowner credit" to reduce customers' bills (*Id.* at 9).
8 MWD argues on brief that its proposed larger plant site will allow a larger buffer area than Arizona-
9 American's proposed site (*Id.* at 12-13).

10 MWD disagrees with Arizona-American regarding the rate impact on Arizona-American's
11 customers if Arizona-American were to purchase capacity from an MWD regional plant as opposed
12 to going forward with its own plans for constructing the White Tanks Project. MWD disputes the
13 assumptions in Arizona-American's analysis regarding MWD recovery of its capital costs (*See* Tr. at
14 217-218; Tr. at 485); regarding the date MWD plant would come on line (*See* Tr. at 218-219;
15 Surrebuttal Testimony of James P. Albu, Exh. D-44 at 7); regarding the amount of land costs that
16 MWD would recover in its charges for treatment services (*See* Tr. at 219; Tr. at 577-78, 221-222,
17 Exh. D-7); and regarding the additional cost to Arizona-American related to use of MWD's plant
18 instead of Arizona-American's White Tanks Project (*See* Tr. at 222-223; Exh. D-44 at 8; Tr. at 142;
19 Exh D-4; Tr. at 125-128). MWD asserts that access to its Agua Fria surface water will be available
20 only at MWD plant (*See* Tr. at 55), and therefore, Arizona-American will be required to build
21 facilities to access MWD's Agua Fria that surface water in any event. In its reply brief, MWD posits
22 that if Arizona-American purchases Agua Fria surface water from MWD, the parties can work
23 together to minimize use of the 60 groundwater wells owned by MWD, but that "[t]he opportunity
24 will be lost if Arizona-American goes it alone and builds a separate plant" (MWD Reply Br. at 9).

25 MWD argues that Arizona-American's plan to construct the plant will lower the Company's
26 equity ratio, and will result in high levels of contributed plant (MWD Opening Br. at 14-15). Based
27 on its view that no hook-up fees are necessary, MWD asserts that it would not be just and reasonable
28 to require increased hook-up fees. MWD also argues that the proposed hook-up fee proposal is not

1 revenue neutral, that the hook-up fees are "rates" and that the Commission cannot adopt Arizona-
2 American's proposed hook-up fee without a fair value finding. MWD does not seem opposed to the
3 concept of a hook-up fee; however, as it suggests that the Commission could approve a hook-up fee
4 to cover the extra cost Arizona-American claims it would incur to purchase treatment capacity from
5 MWD instead of building its own plant (MWD Reply Br. at 11).

6 In its closing brief, MWD alleges that Arizona-American is violating its existing hook-up fee
7 tariff when it requires developers to contribute wells or collect advances for offsite projects (*Id.* at
8 19). MWD is also opposed to Arizona-American's requested accounting orders on the grounds that
9 they are "unprecedented" (*Id.*).

10 MWD requests that the Commission grant it the following relief:

- 11 1) Deny Arizona-American's request to increase its hook-up fee;
- 12 2) Deny Arizona-American's request for an accounting order to accrue AFUDC;
- 13 3) Deny Arizona-American's request for an accounting order to delay recognition
14 of CIAC until related plant is in service;
- 15 4) Deny Arizona-American's request that it be ordered to include a proposal for
16 an O&M Expense Adjustor in its next rate case for its Agua Fria division;
- 17 5) Authorize Arizona-American to reflect the margin credit proposed by MWD
18 on the bills for Arizona-American's Agua Fria Division;
- 19 6) Direct Arizona-American to cooperate in developing and administering the
20 margin credit program;
- 21 7) Order Arizona-American to account for all advances and contributions it has
22 received for off-site facilities beyond those collected through its off-site hook-
up fee after that tariff went into effect;
- 23 8) Order Arizona-American to refund all advances and contributions it has
24 received for off-site facilities beyond those collected through its off-site hook-
up fee after that tariff went into effect; and
- 25 9) If the Commission grants any of Arizona-American's requests, then in the
26 alternative, MWD requests that, in order to protect Arizona-American's
27 customers, the Commission order the following:
 - 28 A) Any hook-up fees collected by Arizona-American should be subject to
refund, should the Commission determine in a rate case that lower fees are

appropriate, or should the courts find the fee increase to be invalid;

- B) To guarantee Arizona-American's ability to make the refund, it should be ordered to post a bond in the amount of the estimated hook-up fee collections for the next five years;
- C) The Commission should make clear that O&M costs for Arizona-American's plant will be evaluated under the Commission's traditional ratemaking methods;
- D) The Commission should rule that no portion of the cost of Arizona-American's plant will be allowed in rate base; and
- E) The Commission should rule that it will not allow an increased cost of capital due to financial weakness caused by Arizona-American building the plant.

C. DEVELOPERS

1. Stipulation Regarding Paid Hook-Up Fees

Courtland, Taylor Woodrow, CHI, Trend, and Arizona-American stipulated that Arizona-American will not impose or seek to impose higher hook-up fees on the following developer projects, for which Arizona-American has entered into Water Facilities Line Extension Agreements ("LXAs") which are at operational acceptance for purposes of the LXAs, and for which the developers have already paid hook-up fees under Arizona-American's existing hook-up fee tariff: Greer Ranch North (Courtland), Sycamore Farms (Taylor Woodrow), Sarah Ann Ranch (CHI), and Cortessa (Trend). The parties further stipulate that any future true-ups to hook-up fees already paid for those developer projects will be based on the Commission-approved tariff that existed at the time the original payment was made. The above-described stipulation was admitted to the record in this proceeding as Hearing Exhibit A-1 ("Stipulation").

CHI, Courtland, and Taylor Woodrow disagree with the statement in MWD's closing brief that adoption of the Stipulation "will result in hook-up fees not being collected from many properties - the same properties that will be the first to develop." CHI, Courtland, and Taylor Woodrow assert that MWD's statement is inaccurate, and that the Stipulation will not result in Arizona-American foregoing revenue to which it otherwise would have been entitled.

Trend also disagrees, stating that the result of the Stipulation would not be to waive collection

1 of hook-up fees, as claimed by MWD, but that it simply provides clarification for developers who
2 have already paid 100 percent of the required hook-up fees.

3 We find the terms of the Stipulation entered by with CHI, Courtland, Taylor Woodrow,
4 Trend, and the Company to be reasonable, because they provide clarification for the Company and
5 for developers who have already paid 100 percent of the required hook-up fees.

6 **2. CHI, Courtland, and Taylor Woodrow**

7 CHI, Courtland, and Taylor Woodrow are all currently developing projects in Arizona-
8 American's Agua Fria District, and have each entered into LXAs with Arizona-American for the
9 provision of water utility service to their projects. CHI, Courtland, and Taylor Woodrow agree that
10 there is an immediate need and necessity for the proposed surface water treatment plant, but take no
11 position on whether Arizona-American or MWD should construct the plant or operate the plant.

12 CHI, Courtland, and Taylor Woodrow request that the Commission's Decision in this matter
13 reflect that Arizona-American may not charge them new hook-up fees to the extent that they have
14 already paid hook-up fees based upon Arizona-American's existing tariff pursuant to the terms of
15 their respective LXAs or other agreements.

16 CHI, Courtland, and Taylor Woodrow also request that the Commission address, in this
17 Decision, three additional issues related to water supply for developers. They request that the
18 Commission preclude Arizona-American from instituting a new service moratorium and require
19 Arizona-American to set meters in circumstances where the developer has supplied the required
20 water to serve the increased demand of a new project.

21 CHI, Courtland, and Taylor Woodrow also request that the Commission order Arizona-
22 American to use its best efforts to work with MWD to obtain both short-term and permanent water
23 supplies to negate (where possible) the requirement that additional wells must be drilled during
24 construction of the surface water treatment plant and thereafter.

25 Lastly, CHI, Courtland, and Taylor Woodrow request that the Commission order Arizona-
26 American to review its existing LXAs and other agreements in the Agua Fria District which require
27 developers to drill new wells in order to determine whether the agreements should be amended to
28 reduce the number of required wells.

1 It is reasonable to require the Company to address the three issues related to water supply
2 raised by CHI, Courtland, and Taylor Woodrow set forth above.

3 **3. Trend**

4 Trend is currently in the process of building homes on lots located in Arizona-American's
5 Agua Fria District, and has paid hook-up fees in association with its development project. Trend
6 requests that the Commission confirm the terms of the Stipulation. As stated above, we find the
7 terms of the Stipulation reasonable.

8 **4. Fulton, Suburban and Westcor/Surprise**

9 Fulton is currently developing a portion of a master-planned community known as Prasada,
10 located in Arizona-American's Agua Fria District. Suburban and Westcor/Surprise are developing a
11 mix of retail centers, a regional shopping center, an auto mall, office complexes, medical facilities,
12 neighborhood grocery and service retail centers, and some medium- to high-density residential
13 components located in Arizona-American's Agua Fria District. Fulton, Suburban and
14 Westcor/Surprise agree that there is an immediate need and necessity for the proposed surface water
15 treatment plant, but take no position on whether Arizona-American or MWD should construct the
16 plant or operate the plant.

17 Fulton, Suburban and Westcor/Surprise take the position that regardless of when the plant
18 becomes operational, Arizona-American should be precluded from instituting a new service hook-up
19 moratorium on any project where the developer provides the "wet" water supply for the particular
20 project pursuant to an LXA between Arizona-American and a developer. They make the same
21 request as CHI, Courtland, and Taylor Woodrow that the Commission's Decision in this proceeding
22 preclude Arizona-American from instituting a new service moratorium in such circumstances, and
23 that the Decision order Arizona-American to continue to set meters at any development that has
24 provided the required water supply for such development pursuant to the terms of the LXA or other
25 agreement between Arizona-American and the developer.

26 Fulton, Suburban and Westcor/Surprise join CHI, Courtland, and Taylor Woodrow in their
27 request that the Commission order Arizona-American to use its best efforts to work with MWD to
28 obtain both short-term and permanent water supplies to negate (where possible) the requirement that

1 additional wells must be drilled during construction of the surface water treatment plant and
2 thereafter.

3 Fulton, Suburban and Westcor/Surprise also join CHI, Courtland, and Taylor Woodrow in
4 their request that the Commission order Arizona-American to review its existing LXAs and other
5 agreements in the Agua Fria District which require developers to drill new wells in order to determine
6 if the agreements should be amended to reduce the number of required wells.

7 Fulton, Suburban and Westcor/Surprise further request that Arizona-American be ordered to
8 review, in conjunction with its review of existing LXAs and before Arizona-American requires
9 developers to drill new wells, less costly alternatives for the utility to supply water for new
10 developments to minimize and otherwise supplant the number of new wells that will need to be
11 drilled in the Agua Fria District, with such review to include the proposed 3.5 mile contingency
12 pipeline alternative in relation to the requirement for new wells to be drilled in the southern portion of
13 the Agua Fria District.

14 The witness for Suburban and Westcor/Surprise testified that in order to meet the current
15 requirements of Arizona-American and MWD, it must drill nine new potable wells in an area where
16 there is poor water quality and capacity (Surrebuttal Testimony of Scott Wagner at 4). Suburban and
17 Westcor/Surprise believe this is attributable to the lack of coordinated effort in the region. Fulton,
18 Suburban and Westcor/Surprise request that the Commission order Arizona-American to coordinate
19 with all interested parties in a regional planning process to assist the Commission in addressing
20 groundwater issues in conjunction with construction of the surface water treatment plant.

21 The additional requests made by Fulton, Suburban and Westcor/Surprise in regard to water
22 supply issues are reasonable, and we will require the Company to address the two additional issues
23 set forth above.

24 **5. Pulte**

25 Pulte is developing or building homes in several locations in Arizona-American's Agua Fria
26 Water District. Pulte states that it supports the expedited construction of a surface water treatment
27 facility in the West Valley. Pulte takes the position that if the hook-up fee request is granted, the
28 amount should not exceed Staff's proposed graduated fees starting at \$3,280 for a 5/8 x 3/4 - inch

1 meter.

2 Pulte also requested, on brief, that the Commission require Arizona-American to insert new
3 language in its tariff to indicate that the hook-up fee changes effective in 2007 will not be charged
4 retroactively, and requiring that hook-up fees be offset by the cost of the off-site facilities (non-
5 distribution facilities) contributed to Arizona-American. Arizona-American responds that the issue
6 of offsetting hook-up fees by the cost of off-site facilities is presently resolved on a case-by-case
7 basis in each developer's LXA. The Company states that the LXA specifies the amount of hook-up
8 fee credit to be applied, if any, and that the LXA is then submitted to the Commission for approval.
9 Arizona-American does not believe that a blanket requirement of a hook-up fee offset is appropriate.
10 The Company argues that alteration of the Company's administration of its hook-up fee offsets is not
11 appropriate in this case, because the issue was not noticed in this proceeding and no evidence has
12 been submitted on the issue.

13 We agree with Arizona-American that there was not sufficient evidence presented on this
14 issue to inform a determination on whether Pulte's request for mandatory hook-up fee offsets should
15 be granted. We note that processes currently exist to aid parties in coming to a resolution of issues in
16 dispute between Pulte and the Company. If parties to an LXA are unable to come to an agreement on
17 LXA issues, the parties may avail themselves of the Commission's informal dispute resolution
18 processes, or may resort to the filing of a formal complaint, if necessary.

19 **D. RUCO**

20 RUCO supports Commission approval of Arizona-American's hook-up fee proposal outlined
21 in the Revised Application to finance the cost of the White Tanks Project. RUCO believes the
22 proposal is in the ratepayers' best interests and is fair to the Company. In support of its position,
23 RUCO states that the Company needs to serve its customers; construction of a treatment plant is
24 necessary to meet the Company's service requirements; the Company is unable to finance the plant at
25 this time; and financing the plant through hook-up fees, which will be treated CIAC, is a cost-free
26 source of financing, which has the effect of lowering customer rates because CIAC is not placed in
27 rate base.

28 Of the two hook-up fee options proposed by the Company, RUCO prefers the second option,

1 which would start at \$4,700 for a 5/8 by 3/4-inch meter, because it would result in smaller accruals of
2 AFUDC, which temporarily flows into customers' rates. RUCO does not object to Arizona-
3 American's proposal to seek, in its upcoming 2008 rate case filing, adjustments to the hook-up fees
4 and a mechanism for recovery of O&M costs, but requests that if the Commission approves this
5 proposal, that the Decision indicate that the Commission is not predetermining the appropriateness of
6 any such hook-up fee modifications or O&M cost recovery mechanism.

7 RUCO states that it has no objection to the issuance of an accounting order as requested by
8 the Company, and that it does not object to the Company seeking adjustments to the hook-up fees and
9 a mechanism to recover O&M costs for the White Tanks Project in its 2008 rate case.

10 RUCO opposes MWD's request to deny the Company's hook-up fee proposal, arguing that
11 the Company, not MWD, is responsible for building the plant necessary to serve its customers.
12 RUCO states that in the event the Commission grants the Company's hook-up fee requests, RUCO
13 does not object to conditions 9(A) and (B) as proposed by MWD. RUCO objects to the remaining
14 conditions proposed by MWD (9(C-E)) on approval of a hook-up fee, based on RUCO's belief that
15 the Commission should not determine the issues raised by those proposed conditions outside of a rate
16 case.

17 RUCO asserts that MWD's request that the Commission compare the Company's and
18 MWD's cost estimates should be rejected as unreasonable and contrary to ratemaking principles.
19 RUCO states that MWD's request constitutes a request for a prudence determination. RUCO argues
20 that the Commission need not, and should not, determine the prudence of the Company's decision to
21 build the White Tanks Project in this proceeding. RUCO argues that while evidence was presented in
22 this proceeding regarding estimated costs, and regarding the parties' respective motivations for
23 building the plant, it is the Company, and not MWD, which is responsible for serving the Company's
24 customers. RUCO is concerned that MWD, as an entity not regulated by the Commission, is not
25 subject to the Commission's oversight, either for the rates it will charge or for future disposal of the
26 plant. RUCO points out that if Arizona-American were to purchase capacity from a plant built by
27 MWD instead of building the plant itself, MWD would have greater bargaining power than the
28 Company, because it would be the sole source of treatment capacity for the area. RUCO states that

1 this situation could lead to unnecessarily high rates for Arizona-American's customers.

2 **E. STAFF**

3 Staff believes that the Commission needs to decide only a single issue in this matter: whether
4 to grant Arizona-American's application to fund construction of a surface water treatment facility
5 through an increase in hook-up fees for the Company's Agua Fria Water District. The Agua Fria
6 Water District is located in an Active Management Area ("AMA"), which makes use of surface water
7 to serve this territory an attractive option for the Company, provided the treatment can be
8 accomplished economically. Staff evaluated the Company's application and determined that
9 Arizona-American's proposal for constructing and financing the plant is a viable proposal. Staff is
10 recommending approval of the Company's requested relief.

11 Staff therefore believes it is unnecessary for the Commission to consider the evidence and
12 analysis presented by MWD regarding its estimates of which entity can more economically build a
13 water treatment facility because MWD is not regulated by the Commission. Staff argues that not
14 only is such consideration of the economic comparison unnecessary, but that it would be
15 inappropriate. Staff points out that the current dispute has come about due to non-cooperation
16 between two competing utility interests, one of which is not regulated. Staff argues that under these
17 circumstances, a Commission determination on the basis of waste to the general public finances
18 would be a very difficult standard to enforce in a regulatory scheme based upon regulated
19 monopolies.

20 Staff argues that a comparison of MWD's proposal with the Company's plan is therefore
21 largely irrelevant. Staff further argues, however, that even if the Commission were to consider such a
22 comparison, Arizona-American's plan is superior, both in design and from a financial standpoint.
23 Staff points out that as of the date of the hearing, MWD's proposal lacked specific detail, even as to
24 its proposed size, and that plans for MWD's proposed plant were not available in any firm form. In
25 contrast, Arizona-American's proposal for a 13.5 MGD plant, consisting of three trains at 6.67 MGD
26 each, has already been designed, competitively bid, and awarded to the lowest bidder. Staff argues
27 that because MWD's proposal lacks specifics and has not been finalized, financial comparison is also
28 difficult. Regarding financing costs, Staff states that the range of interest rates from 3 1/2 to 5

1 percent that MWD claims are available to it would in any event be more expensive than the
2 Company's proposed hook-up fee financing, which is regarded as zero cost capital (*See* Tr. at 647-
3 648). In further support of its position, Staff points to the inability of MWD's financial witness to
4 ascertain that the figures he was given to use as inputs to calculate the rates MWD would charge for
5 water treatment are the actual figures MWD would use in its business dealings with the water
6 companies or with its customers (*See* Tr. at 368-369).

7 Staff is recommending approval of the Company's requested relief, based on its evaluation of
8 the Company's application and Staff's determination that Arizona-American's proposal for
9 constructing and financing the plant is a viable proposal. Staff does not believe that it would be
10 appropriate for the Commission to make a determination regarding whether Arizona-American or
11 MWD should build the regional plant. However, Staff recommends that in the event the Commission
12 were to follow MWD's suggestion to compare cost estimates and somehow "allow" only one plant to
13 be built, Arizona-American's application should also be approved, based on Staff's evaluation that
14 the evidence supports the plant being built by Arizona-American.

15 **III. ANALYSIS**

16 No party disputes that MWD is, as it describes itself, "a critical link in the water supply of the
17 west valley region," or that MWD has provided excellent and low cost service for many years. The
18 Commission respects MWD's record of service to its landowners and its continued commitment to its
19 landowners through its ownership of the Beardsley Canal, creation of Lake Pleasant, and ownership
20 of Agua Fria surface water rights.

21 In the context of this case, however, MWD's speculations regarding the costs of the two
22 "competing" plans for surface water treatment plants are not helpful to our determination whether it
23 serves the public interest to approve Arizona-American's financing proposal. As RUCO states in its
24 reply brief, Arizona-American is not requesting authority to build the plant. The request before us is
25 a narrow one. Arizona-American seeks a grant of authority to institute a method of financing the
26 construction of the White Tanks Project. In no small part due to MWD's participation in this
27 proceeding, we have before us a record that clearly demonstrates the reasonableness and viability of
28 Arizona-American's proposal for constructing and financing the White Tanks Project.

1 No party to this proceeding disagrees with MWD that it has a long history of low utility rates,
2 a public purpose of serving the landowners of MWD, and a democratic structure. MWD argues that
3 these factors demonstrate that MWD would not charge Arizona-American rates for treatment services
4 higher than Arizona-American's cost of service. However, we must take into consideration the facts
5 that MWD's purpose and duty is to serve not Arizona-American's ratepayers, but its landowners, and
6 that MWD is governed by an elected board not subject to the Commission's jurisdiction. In contrast
7 to MWD's duty to its landowners and self-governance structure, Arizona-American is a public
8 service corporation with a legal duty to provide adequate service to its customers at reasonable rates,
9 while subject to the Commission's ratemaking and regulatory authority. MWD is not subject to the
10 same legal obligations regarding rates as Arizona-American. In addition, there is no contractual
11 agreement in place to assure either the Company or the Commission of a firm price that MWD would
12 charge for treatment services. We acknowledge MWD's argument that Arizona-American likewise
13 has not provided MWD a firm treatment price. However, the ramifications of the lack of a firm price
14 differ for a non-regulated versus a regulated entity. While the Commission has ongoing oversight
15 over Arizona-American's facilities and services, if MWD's service rates were to increase in the
16 future, neither the Commission nor Arizona-American's ratepayers would have a means of insuring
17 the reasonableness of the rates.

18 MWD's assertions and arguments do not provide a basis for denial of Arizona-American's
19 request or for the grant of any of the relief requested by MWD, with the exception of MWD's
20 recommendation that hook-up fees should be subject to refund, should the Commission determine
21 that lower fees are appropriate. Similarly, Arizona-American's arguments and assertions do not
22 provide a basis for a finding that it would be imprudent for Arizona-American to purchase treatment
23 services from MWD. Ultimately, it is Arizona American's business decision whether to build its own
24 facility or purchase treatment services from MWD. As with all business decisions of regulated
25 utilities, the prudence of the Company's decision will be subject to examination, if necessary, in a
26 future rate proceeding.

27 **IV. CONCLUSION**

28 Arizona-American is a public service corporation. As a regulated utility, it has an obligation

1 to provide water utility service to its customers at reasonable rates. The Company has demonstrated a
2 need to build the proposed plant and has presented a sound plan by which to finance its construction.

3 We find that it is in the public interest to approve Arizona-American's requests for approval
4 of an increase to its existing Water Facilities Hook-Up Fee, for accounting orders, and for 2008 rate
5 case filing requirements. The record evidence in this proceeding supports approval. We need not,
6 and do not, make a determination here regarding the superiority of one party's plan for a surface
7 water treatment plant over another, or regarding the Company's prudence in exercising its chosen
8 option.

9 * * * * *

10 Having considered the entire record herein and being fully advised in the premises, the
11 Commission finds, concludes, and orders that:

12 **FINDINGS OF FACT**

13 1. Arizona-American is a public service corporation engaged in providing water and
14 wastewater utility services to the public in portions of Maricopa, Mohave, and Santa Cruz Counties,
15 Arizona, pursuant to various Certificates of Convenience and Necessity ("CC&Ns") granted to
16 Arizona-American and its predecessors in interest. The Company presently provides utility service to
17 approximately 100,000 water customers and 50,000 sewer customers in Arizona.

18 2. Arizona-American's Agua Fria District is located in the developing western Phoenix
19 metropolitan area between the White Tank Mountains and the 101 Expressway, mostly to the north of
20 Interstate 10.

21 3. On October 11, 2005, Arizona-American filed the above-captioned application with
22 the Commission.

23 4. By Procedural Order issued December 19, 2005, a procedural schedule was set for the
24 processing of the application, which included a hearing on the application, public notice
25 requirements, and intervention deadlines.

26 5. Intervention was granted to RUCO by Procedural Order issued January 10, 2006.

27 6. On January 23, 2006, the Company filed a Confirmation of Mailing and Affidavit of
28 Publication indicating that public notice of the hearing was accomplished in accordance with the

1 requirements set forth in the December 19, 2005, Procedural Order.

2 7. On February 10, 2006, RUCO filed Direct Testimony of its witness on the October,
3 2005 application.

4 8. Also on February 10, 2006, Staff filed a Staff Report on the October, 2005 application.

5 9. On March 2, 2006, a Pre-Hearing Conference convened at the time set by the
6 December 19, 2005, Procedural Order.

7 10. By Procedural Order issued March 2, 2006, the Company's request that the procedural
8 schedule in this matter be suspended, due to issues that had arisen between the Company and MWD,
9 was granted.

10 11. On September 1, 2006, after the filing of several status reports, and following a
11 Procedural Conference held on August 1, 2006, the Company filed a Revised Application in this
12 docket.

13 12. On September 14, 2006, a Telephonic Procedural Conference was held for the purpose
14 of discussing the appropriate process for a Commission determination in this docket. The Company,
15 RUCO and Staff attended. The parties agreed to confer and either jointly file a proposed procedural
16 schedule, or file separate proposals in the event no agreement was reached.

17 13. On September 25, 2006, Staff filed a Joint Request for a Procedural Order on behalf of
18 Staff, RUCO, and the Company. The Joint Request stated that the parties did not believe, at that
19 time, that an evidentiary hearing was necessary. The Joint Request proposed that Staff file a Staff
20 Report and Staff Recommended Order by October 27, 2006; that the Company and RUCO file
21 responses to the filing by November 6, 2006; and that if there were disputed issues, that a
22 Recommended Opinion and Order be prepared by the Hearing Division.

23 14. On October 5, 2006, a Procedural Order was issued generally adopting the parties'
24 recommendations, and stating that the Hearing Division or the Commission might determine that
25 additional information or a hearing may be required in this matter prior to a Commission Decision.

26 15. On October 27, 2006, Staff filed a Staff Report and Staff Recommended Order,
27 recommending approval of the Company's proposed hook-up fee and accounting order as requested
28 in the Revised Application.

1 16. Between October 23, 2006 and December 6, 2006, Applications to Intervene in this
2 proceeding were filed by Pulte, CHI, Courtland, Taylor Woodrow, Trend, Fulton, Suburban and
3 Westcor/Surprise. These parties were all granted intervention.

4 17. On November 8, 2006, MWD filed an Application for Leave to Intervene.

5 18. On November 29, 2006, the Company filed a Request for Expedited Hearing. In that
6 filing, the Company withdrew its prior opposition to MWD's Application for Leave to Intervene.
7 The Company's Request included a list of issues for hearing and a proposed hearing schedule.

8 19. Intervention was granted to the Developers and MWD.

9 20. On December 13, 2006, a Procedural Order was issued setting a Prehearing
10 Conference for December 21, 2006.

11 21. A Pre-Hearing Conference was held as scheduled on December 21, 2006. Arizona-
12 American, MWD, CHI, Courtland, Taylor/Woodrow, Fulton, RUCO and Staff appeared through
13 counsel and discussed several procedural matters relating to the hearing. The parties also addressed
14 the possibility of settling some disputed issues, and were informed of the necessity of providing
15 notice and an opportunity for participation of all parties in any settlement discussions that might be
16 held.

17 22. On December 21, 2006, a Procedural Order was issued setting a hearing for March 19,
18 2007, and setting associated procedural deadlines.

19 23. On January 11, 2007, the Company filed an Affidavit of Publication verifying that
20 notice of this proceeding was published in accord with the requirements of the December 21, 2006
21 Procedural Order.

22 24. Between January 22, 2007 and March 12, 2007, the parties prefled Direct, Rebuttal,
23 and Surrebuttal testimonies.

24 25. On March 14, 2007, Arizona-American filed an Objection to Data Requests.

25 26. On March 14, 2007, MWD filed a Motion to Strike and Alternative Motion for
26 Expedited Discovery.

27 27. On March 15, 2007, Arizona-American filed its Response to Motion to Strike.

28 28. The hearing in this matter convened as scheduled on March 19, 2007, before an

1 authorized Administrative Law Judge of the Commission, and concluded on March 26, 2007. At the
2 hearing, MWD withdrew its Motion to Strike based on the Company's agreement to provide data
3 responses to MWD. The parties appeared through counsel, presented testimony, and cross-examined
4 witnesses.

5 29. On March 28, 2007, MWD filed Late-Filed Exhibits D-52 and D-53.

6 30. Arizona-American, Pulte, Trend, CHI, Courtland, Taylor/Woodrow, Fulton, Suburban,
7 Westcor, MWD, RUCO, and Staff filed closing briefs.

8 31. On April 27, 2007, reply briefs were filed by Arizona-American, CHI, Courtland,
9 Taylor/Woodrow, Trend, MWD, and RUCO.

10 32. On April 30, 2007, Arizona-American filed a Supplement to Reply Brief.

11 33. Arizona-American requests authorization to record post-in-service AFUDC on the
12 excess of the construction cost of the White Tanks Project (including development, site acquisition,
13 design, company labor, overheads, and AFUDC) over the amount of directly related hook-up fees
14 collected through December 31, 2013, or the date that rates become effective subsequent to a rate
15 case that includes 80 percent (based on estimated cost) of the White Tanks Project in rate base,
16 whichever comes first.

17 34. Arizona-American requests authorization to exclude from rate base the contribution
18 balance of hook-up fees directly related to the White Tanks Project collected subsequent to the
19 effective date of a decision in this case over the aggregate of (1) construction expenditures (including
20 development, site acquisition, design, company labor, overheads, and AFUDC) for the same period
21 that are included in rate base and (2) any costs deemed imprudently incurred from contributions used
22 to calculate rate base until December 31, 2013. The Company's wording "contribution balance of
23 hook-up fees directly related to the White Tanks Project" seems to presume that there may be, at
24 some future date, a balance of hook-up fees that is directly related to the White Tanks Project, but
25 that is not part of the "contribution balance." While the Company may propose, at some future date,
26 some mechanism which may result in such a balance of hook-up fees, there is no such proposal
27 pending, and no Commission determination on such a proposal. Our approval of the Company's
28 request for an accounting order herein should not be viewed as a pre-determination of any future

1 request.

2 35. Arizona-American requests that the Commission require Arizona-American, as part of
3 its 2008 Agua Fria rate case filing, to include a proposal to adjust the Water Facilities Hook-Up Fee
4 Tariff, based on information known to that date, including:

- 5 1) Actual to-date and remaining plant costs;
- 6 2) The effects of any third-party treatment contracts;
- 7 3) Actual hook-up fee collections;
- 8 4) Revised projected customer additions and meter preferences; and
- 9 5) Future Agua Fria Water District capital requirements.

10 36. Arizona-American requests that the Commission require Arizona-American, as part of
11 its 2008 Agua Fria rate case filing, to include a proposed mechanism, similar to the Commission's
12 ACRM procedure, to defer and subsequently recover O&M expense incurred for the White Tanks
13 Project until such expenses can be placed in base rates.

14 37. It is in the public interest to approve Arizona-American's requests for accounting
15 orders.

16 38. It is in the public interest to authorize, but not require, Arizona-American to make the
17 2008 rate case filings it requests.

18 39. Several of the Developers have paid hook-up fees to Arizona-American under
19 Arizona-American's existing Water Facilities Hook-Up Fee Tariff for development projects.

20 40. It is reasonable to require Arizona-American to charge developers for hook-up fees in
21 accordance with the tariffs in effect at the time payment of such fees is required pursuant to the terms
22 of the applicable LXA.

23 41. It is reasonable to require that any true-up of hook-up fees which were paid prior to
24 the effective date of the new Water Facilities Hook-Up Fee Tariff approved by this Decision be based
25 on the hook-up fee tariff in effect at the time the hook-up fee payment was made.

26 42. There is a need for a coordinated potable groundwater procurement program in the
27 Agua Fria District. Accordingly, in order to preserve groundwater resources, as well as to negate the
28 necessity and expense of having additional and possibly redundant wells drilled in the Agua Fria

1 District, it is reasonable to require Arizona-American, as the certificated water service provider in the
 2 area, to coordinate with all interested parties in a regional planning process to address groundwater
 3 issues in conjunction with the construction of a surface water treatment plant.

4 43. It is reasonable to require Arizona-American to address the water supply issues raised
 5 by the Developers, in the manner set forth in the Ordering Paragraphs below.

6 44. The Company requests, and Staff recommends approval of, the following Water
 7 Facilities Hook-Up Fee Tariff:

<u>Meter Size</u>	
5/8 x 3/4-inch	\$ 3,280
3/4-inch	4,920
1-inch	8,200
1 1/2-inch	16,400
2-inch	26,240
3-inch	52,480
4-inch	82,000
6-inch or larger	164,000

12 45. RUCO recommends approval of a Water Facilities Hook-Up Fee Tariff which would
 13 collect higher fees, beginning with \$4,700 for a 5/8 by 3/4-inch meter, because higher fees would
 14 result in smaller AFUDC accruals.

15 46. We find the Water Facilities Hook-Up Fee Tariff recommended by the Company and
 16 Staff to be reasonable, and will adopt it.

17 47. It is in the public interest to approve Arizona-American's request for authorization to
 18 implement the Water Facilities Hook-Up Fee Tariff as discussed herein as a means of financing the
 19 White Tanks Project.

20 48. A hook-up fee tariff has already been approved for the Agua Fria District in Decision
 21 No. 66512 (November 10, 2003). The funds received from the proposed hook-up fees will be
 22 separately recorded as CIAC, and therefore Arizona-American will not be entitled to earn a return on
 23 the hook-up fees. As such, the hook-up fee funds are revenue neutral and will not increase or
 24 decrease the Company's revenues or expenses. Hook-up fees accounted for as CIAC are analogous
 25 to funds received from main extension agreements with developers that are treated as advances in aid
 26 of construction ("AIAC"). Since no fair value determination is made with respect to AIAC funds, a
 27 fair value finding is not required for hook-up fees booked as CIAC.
 28

49. MWD makes a claim that Arizona-American is violating its current hook-up fee tariff. MWD's claim was raised for the first time on brief, and is therefore not properly addressed in this proceeding, which was not noticed as a complaint.

50. The record in this proceeding does not support denial of Arizona-American's requested relief as proposed by MWD.

51. It is appropriate, reasonable, and in the public interest to require that hook-up fees collected under the Water Facilities Hook-Up Fee Tariff approved herein should be subject to refund, should the Commission determine in a future proceeding that lower fees are appropriate.

52. The record in this proceeding does not support the grant of any other relief requested by MWD.

53. The record in this proceeding does not support the request by Pulte to require Arizona-American to institute a blanket policy of offsetting hook-up fees by the cost of contributed off-site facilities. Pulte is not precluded from raising this issue in either an informal or a formal dispute resolution process available at the Commission.

CONCLUSIONS OF LAW

1. Arizona-American is a public service corporation within the meaning of Article XV of the Arizona Constitution and A.R.S. §§ 40-281, 40-282, 40-301 and 302.

2. The Commission has jurisdiction over Arizona-American and the subject matter of the application.

3. Notice of the application was given in accordance with the law.

4. Under the circumstances of this case, and pursuant to Article XV, §§ 3 and 14 of the Arizona Constitution, Arizona-American's proposed Water Facilities Hook-Up Fees, which will be booked as contributions in aid of construction, do not constitute rates that require a fair value determination prior to approval.

5. Under the circumstances of this case, and pursuant to Article XV §§ 3 and 14 of the Arizona Constitution, it is just, reasonable, and serves the public interest to approve the new Water Facilities Hook-Up Fee Tariff as a means of financing the proposed White Tanks Project in accord with the discussion herein.

ORDER

IT IS THEREFORE ORDERED that the application of Arizona-American Water Company for authority to implement a Water Facilities Hook-Up Fee Tariff in accord with the discussion herein as a means of financing the White Tanks Project shall be, and hereby is, approved.

IT IS FURTHER ORDERED that funds collected pursuant to the Water Facilities Hook-Up Fee Tariff approved herein are subject to refund in the event that the Commission determines in a future proceeding that lower fees are appropriate.

IT IS FURTHER ORDERED that with the exception of the preceding Ordering Paragraph, which partially grants relief requested by the Maricopa County Municipal Water District Number One, the relief requested by the Maricopa County Municipal Water District Number One shall be, and hereby is, denied.

IT IS FURTHER ORDERED that this Decision does not predetermine the appropriateness of any modifications proposed in the future to the Water Facilities Hook-Up Fee Tariff approved herein.

IT IS FURTHER ORDERED that Arizona-American Water Company's request for authorization to record post-in-service allowance for funds used during construction on the excess of the construction cost of the White Tanks Project (including development, site acquisition, design, company labor, overheads, and allowance for funds used during construction) over directly related hook-up fees collected through December 31, 2013, or the date that rates become effective subsequent to a rate case that includes 80 percent (based on estimated cost) of the White Tanks Project in rate base, whichever comes first, shall be, and hereby is, approved.

IT IS FURTHER ORDERED that Arizona-American Water Company's request for authorization to exclude from rate base the contribution balance of hook-up fees directly related to the White Tanks Project collected subsequent to the effective date of this Decision over the aggregate of (1) construction expenditures (including development, site acquisition, design, company labor, overheads, and allowance for funds used during construction) for the same period that are included in rate base and (2) any costs deemed imprudently incurred from contributions used to calculate rate base until December 31, 2013, shall be, and hereby is, approved.

IT IS FURTHER ORDERED that Arizona-American Water Company is hereby authorized to

1 file, as part of its 2008 Agua Fria Water District rate case filing, a proposal to adjust the Water
2 Facilities Hook-Up Fee Tariff approved herein. If such a proposal is filed, it shall include
3 information necessary to allow the Commission to adjust the Water Facilities Hook-Up Fee Tariff as
4 necessary, based on the best information available at the time, including, but not limited to, the
5 following:

- 6 1) Actual to-date and remaining plant costs;
- 7 2) The effects of any third-party treatment contracts;
- 8 3) Actual hook-up fee collections;
- 9 4) Revised projected customer additions and meter preferences; and
- 10 5) Future Agua Fria Water District capital requirements.

11 IT IS FURTHER ORDERED that Arizona-American is hereby authorized to file, as part of its
12 2008 Agua Fria Water District rate case filing, a proposed mechanism to defer and subsequently
13 recover Operations and Maintenance Expense incurred for the White Tanks Project until such
14 expenses can be placed in base rates.

15 IT IS FURTHER ORDERED that this Decision does not predetermine the necessity for or the
16 appropriateness of any mechanism proposed in the future by Arizona-American Water Company for
17 recovery of Operations and Maintenance Expense incurred for the White Tanks Project.

18 IT IS FURTHER ORDERED that the request by Pulte Homes Corporation to require
19 Arizona-American Water Company to institute a blanket policy of offsetting hook-up fees by the cost
20 of contributed off-site facilities shall be, and hereby is, denied.

21 IT IS FURTHER ORDERED that Arizona-American Water Company shall charge
22 developers for hook-up fees in accordance with the tariffs in effect at the time payment of such fees is
23 required pursuant to the terms of the applicable line extension agreement.

24 IT IS FURTHER ORDERED that any true-up of hook-up fees which were paid prior to the
25 effective date of the new Water Facilities Hook-Up Fee Tariff approved by this Decision shall be
26 based on the hook-up fee tariff in effect at the time the hook-up fee payment was made.

27 IT IS FURTHER ORDERED that Arizona-American Water Company shall be, and hereby is,
28 precluded from instituting a new service moratorium on the initial hook-ups in circumstances where

1 the developer has supplied the required water to serve the increased demand of a new project
2 pursuant to a line extension agreement.

3 IT IS FURTHER ORDERED that Arizona-American Water Company shall review its
4 existing line extension agreements in the Agua Fria Water District that require developers to drill new
5 wells, in order to determine whether it is feasible to amend those line extension agreements to reduce
6 the number of required wells, in cooperation with the parties to those line extension agreements.

7 IT IS FURTHER ORDERED that, in conjunction with the review of line extension
8 agreements required by the previous Ordering Paragraph, Arizona-American Water Company shall
9 consider whether there exist less costly alternatives for the utility and the developers to supply water
10 for new developments in order to minimize and otherwise supplant the number of new wells that will
11 need to be drilled in the Agua Fria District. In the course of this review, Arizona-American Water
12 Company shall consider a proposed 3.5 mile contingency pipeline alternative in relation to the
13 requirement for new wells to be drilled in the southern portion of the Agua Fria District.

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1 IT IS FURTHER ORDERED that Arizona-American Water Company shall use its best
 2 efforts to coordinate with all interested parties, including the Maricopa County Municipal Water
 3 District Number One, in a regional planning process to obtain both short-term and permanent water
 4 supplies to negate, where possible, the need to drill additional wells during construction of a regional
 5 surface water treatment plant to serve the Agua Fria Water District.

6 IT IS FURTHER ORDERED that this Decision shall become effective immediately.

7 BY ORDER OF THE ARIZONA CORPORATION COMMISSION.
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 9

10 CHAIRMAN _____ COMMISSIONER _____

11
 12 COMMISSIONER _____ COMMISSIONER _____ COMMISSIONER _____

13
 14 IN WITNESS WHEREOF, I, DEAN S. MILLER, Interim
 15 Executive Director of the Arizona Corporation Commission,
 16 have hereunto set my hand and caused the official seal of the
 Commission to be affixed at the Capitol, in the City of Phoenix,
 this ____ day of _____, 2007.

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 18 _____
 DEAN S. MILLER
 INTERIM EXECUTIVE DIRECTOR

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 20 DISSENT _____

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 22 DISSENT _____

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